CITY OF SAN JOSE
DEFERRED COMPENSATION PLAN
A BENEFIT FOR YOUR FUTURE

DEFERRED COMPENSATION
INVESTMENT SUBCOMMITTEE

The Deferred Compensation Ad-Hoc Investment Sub-Committee meeting was called to order at 10:40 a.m. on Wednesday, June 11, 2008, City Hall, Wing, W118.

Roll Call

Donna Busse	Management Employees' Representative (392-6709)
Julia Cooper	City Manager's Representative (535-7011)

Also Present

Suzanne Hutchins	City Attorney's Office
Bill Tugaw	Consultant, SST Benefits (650) 940-1111
Jeanne Groen	Human Resources, Deferred Compensation Secretary
Courtney Phommachack	Human Resources, Deferred Compensation Staff
Chuck Sklader	Consultant, SST Benefits (480) 991-8588
Gary Bozin	ING
Bruce De Mers	Retiree

Excused Absence

Conrad Taylor	Police Representative (POA 277-4012)

AGENDA

10: 30 AM. **June 11, 2008** **City Hall, Wing 118**

APPROVAL OF MINUTES

1. M.S.C. (Busse/Cooper) to approve minutes for the May 21, 2008 meeting.

NEW BUSINESS

2. Revised Performance Sheet Update

Jeanne Groen reported that at the last subcommittee meeting direction was given to go back and align our Deferred Comp investment returns to include the categories that a participant could cross walk over to the investment policy.

A handout of the first draft of the "Deferred Compensation Investment Returns" was sent to the subcommittee. Jeanne explained that last night she, Bill Tugaw and Chuck Sklader had a conversation regarding the returns. Chuck Sklader recommended that we take the funds that are the index funds, Vanguard Institutional Index Fund, Vanguard Mid-Cap Index and Vanguard Small-Cap Index Fund and compare them to the Large Cap Blend, Mid Cap Blend and Small Cap Blend as appropriate. This would allow participants to compare funds that are alike. Chuck Sklader had also indicated that when we do an RFP for funds we look at Index as a category and we look at them together; however, when we are comparing the return rates it would be more appropriate for a participant to look at blended Large Cap, Mid Cap and Small Cap. As a result of this conversation, staff provided an alternative that is dated June 10, 2008 with the revisions. For example, the Vanguard Institutional index is listed under the Large Cap Blend. The Vanguard Mid – Cap Index is under the Mid Cap Blend and the Vanguard Small Cap Index is under the Small Cap Blend. The funds track a little better to like funds, making it easer for participants to review comparable performance. The option is to either keep the Index funds separate or to compare them to the blended funds.

Bill Tugaw stated that one of the things that SST does in their normal review is to compare active managers versus passive managers. Bruce DeMers asked Bill Tugaw about performance reports that also include the category "average". Bill Tugaw responded that they use the category "average" in the annual fund review. SST provides a copy annually and employees can get this information on the City's website. Bill Tugaw further explained that SST analyzes by style of fund managers. SST compares against category peer group averages rather than index but SST also shows an index comparison because there are a lot of people that want to see it compared to an index. So both types of comparisons are done, however if you try to show all of that on the Performance Update Sheet it will be too busy for participants to understand. There are a lot of numbers on the sheet already.

The committee concurred that the revised version of the "Deferred Compensation Investment Returns" is better. Member Busse inquired if any action is required. Member Cooper also wondered if this needs to be reported out to the DCAC. Jeanne Groen and Suzanne Hutchins concurred that this is a staff issue and it's just a recommendation to staff.

3. <u>Review current loan provisions</u>

Jeanne Groen stated that at the last meeting there was a question as to whether the investment policy and the contract currently match and whether it was the DCAC's intent to require loan repayment upon termination. Jeanne explained that she went back to DCAC minutes to review if the DCAC had approved that a loan balance would have to be paid off at the time an employee terminated. The April 26, 2007 minutes contain approval of a draft ordinance to implement loan provisions in the Deferred Compensation Plan and authorization for the staff to negotiate a loan program custody agreement with ING. Part of that discussion was that Susan Devencenzi provided the committee direction to make some changes. The third bullet in the minutes stated:

> 3.48.140 (G): Delete the word "immediately" in the second sentence and add additional language such as "due and payable no later than the last day of the month immediately following the month in which participant receives his or her final compensation from the City. Final compensation includes any payments for unused accrued leave for which the participant may be eligible.

The actual Loan Program Custody Agreement between the City of San Jose and ING National Trust with this loan repayment information came back to the DCAC and was approved at the August 23, 2007 DCAC meeting. So, the Loan provisions contained in the Investment Policy is correct.

Bruce DeMers inquired about previous discussions on the repayment of loans after retirement. He thought they had set up payments after retirement. Bill Tugaw responded that he remembers the conversation and at that time they were discussing potential options that the DCAC could explore with ING. He explained that 30 days pay off after final compensation is pretty much standard.

Jeanne Groen stated that the investment policy is correct and matches the DCAC minutes.

OLD BUSINESS

4. Review and discuss revised draft Investment Policy and Procedures Statement.

The Subcommittee agreed to review the proposed revised version of the Investment Policy and Procedures Statement dated June 11, 2008. Jeanne Groen stated that she provided the changes made since April. Since it was easier to provide a clean copy, she highlighted all the changes that occurred since the last update. This is the proposed final. A final check does need to be made for typos.

Page 1: Jeanne Groen explained that she added to the first paragraph “may change” Suzanne Hutchins suggested changing to “and may change”. Everyone agreed that would make the sentence clearer. The second paragraph was changed to make it more generic from “the plan may offer up to 15 investment categories” to “a variety of investment categories, all of which”. The word “investment” was added before “vehicles” in the last paragraph.

Page 2: Numbers were added to make it easier to read because it was a very long sentence.

Page 5: The paragraphs entitled “Socially Responsible Investing” and “Specialty Funds” were reviewed. On the last sentence “and” was added before “controlling”.

Page 7 Tables: Jeanne Groen reported that there was a request that we make the tables more consistent with our categories. Staff added the “Socially Responsible Investment (SRI)” and “Specialty Fund”. Chuck Sklader suggested that to make it clearer to the participant that the DCAC and Investment Subcommittee does not monitor the self directed brokerage accounts and he did not want to see it in this table because those are the core offerings that are reviewed and approved by the DCAC. Staff did want to provide the information to the participant, so staff set up a separate table added some language above that. Everything under “Socially Responsible Investment (SRI)” and “Specialty Fund” has been added. There are some typos to be corrected and the column widths need to be fixed.

Page 11: This table used to be a number of boxes that went over a couple of pages. Jeanne Groen explained she just put the information into a different table format. There are a couple of areas where she and Chuck Sklader made a couple of recommendations. Asset Allocation Fund – 6 to 8 funds. Bill Tugaw added that this is about as many as you can get. Socially Responsible Investment Fund: 1 to 2 Funds. Self Directed Brokerage Account – Limited to 50% of Account to specified retail fund list, individual stocks and bonds.

Member Cooper commented that since we're up to 3 asterisks perhaps we should number them. Jeanne Groen responded that she would.

Page 12: Jeanne Groen reported that this section was reworded to address whether the section is for initial funds or current funds and how each are handled. This is new language that's being proposed for review.

Page 13: Member Busse commented that the last sentence in first paragraph is confusing: "Current funds will be evaluated against the peer group. For all funds, including a new fund or deleting an existing fund in the Plan may also occur for the following reasons:" She inquired if we're dealing with two different things in one paragraph, deleting the existing and hiring a new one?

Bill Tugaw explained that you can divide that into two separate sections because we're talking about the screening of a new fund and then tagging on to that the screening that happens to all funds. Member Busse asked if reviewing the current funds is part of the screening process for evaluating a new fund. Bill Tugaw responded that it is. Member Busse inquired if, in order to evaluate a new fund, do you have to screen the old funds? We have the current review in a separate section. This should have already been done and this should be about the new fund.

Jeanne Groen asked when we do a fund review, do we rank them? Bill Tugaw responded that in the review, SST does rank the fund. Member Busse states that unless comparing the new funds with the current funds is part of the evaluation process then it doesn't belong here.

Member Cooper noted that we are doing two separate things in this section. Looks like we're supposed be looking at a process for selecting to add a new fund. Then there is a completely separate process to do the annual review of funds. It appears there should be two separate processes. Bill Tugaw explains that there is a review of the entire portfolio on an annual basis and that is where we start. As a fund fails in the annual review, this is where we decide why it failed. Is it acceptable based on our research or do we want to delete it? That is actually the secondary step of the same process.

Member Busse states that once you've made a determination there should be a clean process of selecting a new fund or if you want to add a new fund and not terminate a fund. Julia Cooper states that we should start with the annual review process and do that first and then we'll go back and do the initial review for adding a new fund.

Member Busse said that we should have a process to put a new fund in place, then you have a review in place for your existing portfolio, and then you have a process to put a fund in your portfolio whether it's by termination of another one or adding a new category. It should be able to cover all situations. The steps are all ok, but she is just getting confused with the mixing of the new funds with the current funds. The processes don't have to be linked as long as there is a process for selecting a fund and a process for terminating a fund. She explained that she thought a, b, and c were all part of adding a new fund and Page 18 and 19 was the reviewing process of the existing portfolio.

Member Cooper suggested taking "Investment Fund Evaluations" section that starts on page 18 and putting that ahead of the "Investment Fund Selection" process. You're going through the annual review and then you may have to do this for a screening process to replace somebody or you may be doing the screening process because you're adding a new category mid annual evaluation process. But in reality, this is in conjunction with the annual process unless something comes up that is catastrophic and you need to get rid of a fund right away. Member Busse comments that the hiring process should be same regardless of the reason you are hiring somebody. If you move 18 and 19 in front, the policy should be ok.

Jeanne Groen responds that back on page 13, we'll delete the sentence that says "Current funds will be evaluated against the peer group." Member Busse suggested that in the second sentence referencing new funds should be removed but that the reason for evaluating a fund be kept in.

Page 16: The graph shows 3 and 5 year standards. Jeanne Groen asked if the 1 year standard was the same. Bill Tugaw responded that the one year standard is the same. Jeanne Groen will check and if they are all the same she will correct the columns. The International Equity Funds and the "Global Equity Funds" were also added. In the previous graph there was "International/Global. Chuck Sklader thought it might be clearer if we separated the two.

Page 17: In last three funds "Specialty Funds, "Real Estate Funds" and Socially Responsible Funds" the words changed slightly and on the "Asset Allocation Funds" so the revised language is highlighted for review.

Bruce DeMers inquired about the Asset Allocation Funds and Bill Tugaw responded that these funds are so new that the actual benchmarks are very hard to determine because different fund families are putting the funds together differently. Bill Tugaw reports that ING is working on it. Every one of the Asset Allocation models we have is comprised of the underlying funds that are already in your portfolio so when SST does the analysis of the portfolio, by definition, we are analyzing every fund that's in the asset allocation models. It's very difficult to figure out how to benchmark these funds because they are all different. There's article after article on how you do this and how you compare them. Because SST has analyzed the underlying funds, we're ok with the fund there but we need to take a look at the design of the actual model itself and get into that. For this group, for right now, Bill Tugaw suggests that the Subcommittee wait and let another SST client head down that path first.

Page 19: Member Busse says she thinks we repeated a paragraph on page 19 at the end of the paragraph on page 22. On page 19 it states: "The Deferred Compensation Plan will be reviewed according to the criteria outlined in this Investment Policy no less frequently than annually. However, conditions may arise that create a need for an evaluation on a more frequent basis." Then, on page 18, "Conditions may arise that create a need for an evaluation on a more frequent basis." It's like part of 22 and part of 18 on page 19. Staff was directed to beef up 18 and 22 to resolve the issue.

Jeanne Groen comments that Suzanne Hutchins had a comment under 19. Consultant Provider should be in lower case because we haven't defined them. She also suggested we use the word Benefits Consultant to make it clearer. Bruce DeMers suggested Deferred Comp Consultant and Bill Tugaw agreed. Jeanne Groen will also replace provider with Investment Provider.

Page 12: Bill Tugaw suggested in the last paragraph to scratch "benefits" before consultant.

Member Busse inquired if it's ok to go forward.

Page 5: Gary, last sentence says "matters that they are capable of making, managing controlling." He recommended changing this to "managing and controlling."

Member Cooper comments that on the agenda language which says review and discuss. She suggested that the Subcommittee send the Investment Policy to the full DCAC Committee with the changes we worked on today without a recommendation.

PUBLIC COMMENTS

None.

ADJOURNMENT

M.S.C. (Busse/Cooper) to adjourn the meeting at 11:20 a.m.

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Donna Busse
Investment Subcommittee Member

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Julia Cooper
Investment Subcommittee Member